United States Court of Appeals

for the Second Circuit

APPENDIX

Signed

77-4179

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Pgs

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

WILLIAM J. McDONALD, SR., and ELIZABETH J. McDONALD,

Appellees

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellant

ON APPEAL FROM THE DECISION OF THE

UNITED STATES TAX COURT

APPENDIX

M. CARR FERGUSON,
Assistant Attorney General,

GILBERT E. ANDREWS,
WILLIAM S. ESTABROOK,
THOMAS M. WALSH,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

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UNITED STATES TAX COURT

WILLIAM J. MC DONALD, JR., and
ELIZABETH J. MC DONALD,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Petition

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (AP:BUF:[illegible]) dated April 9, 1976 and as the basis for their case allege as follows:

1. The petitioners are individuals with residence at 870 Pre-Emption Road, Geneva, New York, 14456. The returns for the periods herein involved were filed with the Internal Revenue Service at 310 Lowell Street, Andover, Massachusetts for the Buffalo District of New York State.

2. The notice of deficiency (a copy of which, including so much of the statement and schedules accompanying the notice as is material, is attached and marked "Exhibit A") was mailed to the petitioners on April 9, 1976 and was issued by the office of the Internal Revenue Service at Buffalo, New York.

3. The deficiencies as determined by the Commissioner are in income taxes for the calendar years 1970, 1971, 1972 and 1973 in the amount of $33,939.60 all of which is in dispute

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

a. The Commissioner disallowed the deduction of $121,400.00 paid for preservation of the reputation of the taxpayer, William J. McDonald, Sr. as an attorney, stating that it was not an allowable deduction under any provision of the Internal Revenue Code of 1954.

5. The facts upon which the petitioners rely as the basis of this case are as follows:

a. Hazel A. Leckie died on the 28th day of February, 1972. Her will appointed the taxpayer William J. McDonald, Sr., executor and left the taxpayer and his wife several bequests and the residue of her estate. When the will was offered for probate, objections were raised to the probate by relatives of Mrs. Leckie, stating that the bequests to the taxpayer and his wife were not freely or voluntarily made by Mrs. Leckie but were procured by the undue influence practiced upon her by the taxpayer, William J. McDonald, Sr.

b. Thereafter, Letters of Administration were issued to William J. McDonald, Sr., without bond.

c. On November 15, 1972, the objections were withdrawn and the will was admitted to probate. Thereafter a compromise agreement dated December 12, 1972 was finally executed by all of

the parties in April of 1973.

d. Under the agreement, the taxpayer, William J. McDonald, Sr., agreed to take certain payments which payments are the deduction disallowed by the Commissioner. The agreement recited that the reason for the payments, i.e. the agreement, was that:

"Litigation of the issues would engender much publicity and would cast upon the reputation of William J. McDonald as an attorney."

e. That thereafter and on April 23, 1973, the Surrogate approved the compromise agreement and in the order set forth the following:

"That the compromise agreement and all other papers pertaining to this proceeding shall be sealed and shall not be subject to access or inspection except by order of the Surrogate for a good cause shown and on notice to William J. McDonald."

f. The trial involving allegations of undue influence which was prevented by the payment of the money in question would have engendered much publicity.

g. The taxpayers had received an anonymous letter in regard to the situation.

h. The taxpayer, William J. McDonald, Sr., has been a lawyer since 1950. He has an "A" Rating in Martindale-Hubbell. He is a past president of the local Bar Association, a longtime member of the Executive Committee of the Trial Lawyer Section of the New York State Bar Association, a former head of the Ethics Committee of the local Bar Association for about fifteen years, the present president of the Parish

Council, trustee and secretary of the Board of Trustees of Geneva Growth, Inc., and, in addition thereto, he has had many other positions throughout the years of private and public trust.

i. In a small town, the worth of this type of reputation in a law practice is incalculable.

j. The taxpayer had been told that one of the attorneys for the objectants had stated that he would do anything he could to get the taxpayer, William J. McDonald, Sr.

k. The same attorney had made a complaint to the State Bar Association in regard to the situation after the settlement had been made.

l. Decedent, Hazel A. Leckie, the taxpayer and his lawfirm were well known in the City of Geneva which has approximately 17,000 population.

m. The decedent, Mrs. Leckie, had written notes which, if published, would have greatly damaged the taxpayer's reputation.

WHEREFORE, petitioners pray that this court may try the case and make a determination that no deficiency exists as to the taxpayers for the taxable years 1970, 1971, 1972 and 1973 together with costs.

Dated: June 4, 1976

/s/William J. McDonald
William J. McDonald

/s/Elizabeth J. McDonald
Elizabeth J. McDonald

870 Pre-Emption Road
Geneva, New York 14456
Tel: AC 315 789-1310

UNITED STATES TAX COURT
WASHINGTON, D.C. 20217

1977 FEB 11 PM 4 32

WILLIAM J. MC DONALD, SR., and ELIZABETH J. MC DONALD, Petitioners	
v.	Docket No. 5160-76
COMMISSIONER OF INTERNAL REVENUE, Respondent.	

ORDER

The parties in the above-entitled case having filed on February 8, 1977, a joint motion for submission of this case under Rule 122, Tax Court Rules of Practice and Procedure, with accompanying stipulation of facts, it is

ORDERED: That the proceeding be and the same hereby is assigned to Judge Howard A. Dawson, Jr., for disposition. Opening briefs will be due from both parties on March 28, 1977, and reply briefs will be due on April 27, 1977.

(Signed) HOWARD A. DAWSON, JR.

Howard A. Dawson, Jr.
Chief Judge

Dated: Washington, D.C.
February 11, 1977

RECEIVED IN
MAR 7 1977
Regional Counsel's Office
Buffalo

Initialed Copy

Sent to the Tax Court FEB 8 1977

UNITED STATES TAX COURT

WILLIAM J. MC DONALD, SR., AND ELIZABETH J. MC DONALD,	)	
Petitioners,	)	
v.	)	Dkt. No. 5160-76
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

RECEIVED IN

FEB 11 1977

Regional Counsel's Office
Buffalo

JOINT MOTION FOR LEAVE TO SUBMIT CASE UNDER RULE 122

THE PARTIES JOINTLY MOVE for leave to submit the above-entitled case under Rule 122 of the Court's Rules of Practice and Procedure, and request that the case be assigned to a Division of the Court for report.

THE PARTIES FURTHER MOVE that they be granted leave to file simultaneous briefs, with opening briefs due MAR 28 1977 and reply briefs due APR 27 1977

IN SUPPORT THEREOF, the parties respectfully show unto the Court:

The parties are in agreement that the above-entitled case does not require a trial for the submission of evidence, and that accordingly the case may be submitted upon the basis of the pleadings and the facts recited in the stipulation of facts

(with exhibits thereto), which is being filed concurrently with this motion.

WHEREFORE, it is prayed that this motion be granted.

WILLIAM J. MC DONALD, SR.
Petitioner

ELIZABETH J. MC DONALD
Petitioner
870 Pre-Emption Rd.
Geneva, N.Y. 14456

CHARLES L. SAUNDERS, JR.
Acting Chief Counsel

By: Stephen M. Miller
STEPHEN M. MILLER
Assistant Regional Counsel
304 U.S. Courthouse
Buffalo, N.Y. 14202
Tel. No. 716-842-6834

Date: FEB 3 1977

UNITED STATES TAX COURT

WILLIAM J. MC DONALD, SR. and ELIZABETH J. MC DONALD,	)	
Petitioners,	)	
v.	)	Dkt. No. 5160-76
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto that, for purposes of this case, the following statements are accepted as facts, and the exhibits referred to herein and attached hereto are incorporated in this stipulatior and made a part hereof.

1. Petitioners are husband and wife who resided at 870 Pre-Emptior Road, Geneva, New York 14456, at the time of the filing of the petition herein.

2. Petitioners timely filed their federal income tax returns for the taxable years 1970 through 1973 with the Internal Revenue

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Service Center at Andover, Massachusetts. True and complete copies of these returns are attached hereto as Joint Exhibits 1-A through 4-D.

3. Petitioner William J. Mc Donald, Sr. (hereinafter referred to as "petitioner") is an attorney who was admitted to the practice of law in the State of New York in 1950. He is presently actively engaged in law practice as a member of the firm of Bond, Mc Donald & Toole, 435 Exchange Street, Geneva, New York 14456.

4. On August 21, 1968, Hazel A. Leckie executed her last will and testament, a copy of which is attached hereto and marked Joint Exhibit 5-E. This document was not drafted by petitioner.

5. On November 6, 1970 Hazel A. Leckie executed a codicil to her last will and testament. A copy of this codicil, which was drafted by petitioner, is attached hereto and marked Joint Exhibit 6-F.

6. Hazel A. Leckie died on February 28, 1972.

7. When the Last Will and Testament of Hazel A. Leckie was offered for probate, objections were raised by relatives of Mrs. Leckie who alleged that the bequests to the petitioners

made therein had not been freely or voluntarily made by Mrs. Leckie, but had been procured by undue influence practiced upon her by petitioner William J. McDonald, Sr.

8. Thereafter, letters of administration, without bond, were issued by the Surrogate Court of Ontario County, New York, to petitioner, who had been appointed executor of Mrs. Leckie's estate in paragraph 7 of her Last Will and Testament.

9. On November 15, 1972, the objections to Mrs. Leckie's will were withdrawn and the will (and codicil) were admitted to probate on that date.

10. A written compromise agreement, dated December 19, 1972, was executed by all parties to the dispute and filed with the Surrogate Court of Ontario County. A copy of said agreement, which was finally executed by all the parties and verified on April 12, 1973, is attached hereto and marked Joint Exhibit 7-G.

11. On April 12, 1973, petitioner filed with the Surrogate Court of Ontario County a "Petition for Order Approving Compromise of Controversy", a copy of which is attached hereto and marked Joint Exhibit 8-H.

12. On April 23, 1973, Hon. Joseph W. Cribb, Surrogate of Ontario County, signed an order approving the aforementioned compromise agreement. A copy of this Order is attached hereto and marked Joint Exhibit 9-I.

13. During 1973, petitioner paid the sum of $121,400. which he had received under the residuary clause of the last will and testament of Hazel A. Leckie. Petitioner paid this sum to the heirs and relatives of Mrs. Leckie under the terms of the aforementioned compromise agreement.

14. Petitioner made the aforementioned payments in order to head off litigation in connection with the will contest proceeding and to avoid any publicity resulting from same.

15. Since 1950, petitioner has served as president of Onatrio County Bar Association, chairman of the Ethics Committee of the Ontario County Bar Association, and as a member of the Executive Committee of the Trial Lawyers Section of the New York State Bar Association, among other things, in connection with his career as a practicing attorney in the Geneva, New York area. He has an "A" rating in Martindale-Hubbell.

(Respondent notes, for the record, his objection to the subject matter contained in paragraph 15 as irrelevant to the issue in this case).

16. On their 1973 income tax return, petitioners claimed a miscellaneous itemized deduction of $121,400.00 for "preservation of reputation", attaching an explanation and copies of two

canceled checks totaling $121,400.00 payable to BONNEY & NICIT, attorneys for the Will contestants.

17. Attached hereto and marked Joint Exhibits 10-J and 11-K are copies of newspaper articles published in the Geneva, N.Y., Times on June 17, 1976, and the Rochester Democrat and Chronicle on June 15, 1976, respectively.

Note: While the parties stipulate to the authenticity of these documents and to the dates and places of publication, neither party stipulates to the truth or falsity of the matters reported therein.

18. On April 12, 1974, petitioners applied for refunds of taxes paid for the taxable years 1970, 1971, and 1972 in the amounts of $6,813.40, $8,263.36, and $1,229.83, respectively. A complete copy of said application is attached hereto as Joint Exhibit 12-L. On July 29, 1974, petitioners' application was granted, and they received refunds of $6,813.40 for 1970, $8,380.37 for 1971, and $1,229.83 for 1972, plus interest.

19. The deficiencies determined by respondent for the taxable years 1970 through 1972 are a result of the disallowance of the carryback of the net operating loss claimed for 1973,

since said loss was occasioned by the claiming of the "preservation of reputation" deduction.

WILLIAM J. MC DONALD, SR.
Petitioner

ELIZABETH J. MC DONALD
Petitioner
870 Pre-EMption Rd.
Geneva, N.Y. 14456

CHARLES L. SAUNDERS, JR.
Acting Chief Counsel

By: (Sgd) Stephen M. Miller

STEPHEN M. MILLER
Assistant Regional Counsel
304 U.S. Courthouse
Buffalo, N.Y. 14202
716-842-6834

Date FEB 3 1977

LAST WILL AND TESTAMENT

I, HAZEL A. LECKIE, being a resident of the City of Geneva, County of Ontario and State of New York, do hereby make, publish and declare this to be my last will and testament.

1. I direct that all of my just debts and funeral expenses be paid as soon as practicable after my death.

2. I direct that my Executor pay out of my residuary estate without apportionment, all estate, inheritance and like taxes imposed by the government of the United States, or any state or territory thereof, or by any foreign government or political subdivision thereof, in respect of all property required to be included in my gross estate for estate or like tax purposes by any such governments, whether the property passes under this will or otherwise, without contribution by any recipient of any such property.

3. To the individuals listed below, I bequeath the following:

A. To my niece, MARY ELIZABETH OLSCHEWSKE, of Waterloo, New York, if she shall survive me, the sum of TEN THOUSAND DOLLARS ($10,000.00).

B. To my employee of many years service, ROSE CONTINI, if she shall survive me, the sum of TEN THOUSAND DOLLARS ($10,000.00).

C. To my friend, WILLIAM J. McDONALD, an attorney of Geneva, New York, if he shall survive me, my "Booth" painting by John Singer Sargent.

D. To my friend, ELIZABETH J. McDONALD, wife of said attorney, all of my jewelry of every kind and description, and all of my furs, if she shall survive me.

E. To ROBERT ROSE, a relative of my former husband, Walter Rose, the chest of silver, bearing the Rose family crest, and also the two black onyx seal rings of the Rose family, if he shall survive me.

F. To MALCOLM SAWTELLE, another relative of Walter Rose, the family painting entitled "Father Jay", if he shall survive me.

G. To MURIEL SAWTELLE, his mother, the family painting entitled "Widow Rousby", if she shall survive me.

H. To WARDELL AYRAULT and ROBERT ROSE, in equal shares, if they shall survive me, all of the remaining paintings of the Rose and the Ayrault family ancestors owned by me at the time of my death; and in the event that one of them shall not survive me, I bequeath all of said remaining Rose and Ayrault family ancestor paintings to the one of them that shall survive me.

4. Under the provisions of a Trust Agreement, dated July 22, 1965, by and between my late husband, ANDREW F. LECKIE, SR., the grantor, and THE HUNTINGTON NATIONAL BANK OF COLUMBUS, OHIO, the Trustee, I was given a power to direct the disposition of certain property. I hereby exercise the said power of appointment granted to me by said instrument, and direct that all property subject thereto shall become and be a part of my residuary estate, and disposed of as hereinafter provided.

5. All of the rest, residue and remainder of the property which I may own at the time of my death, real and personal, and including any property over which I may have any power of appointment, I bequeath and devise to my said friend and attorney, WILLIAM J. McDONALD, of Geneva, New York, if he shall survive me, absolutely and forever. In the event that he shall not survive me, I bequeath and devise all of the said residue of my estate to his wife, ELIZABETH J. McDONALD, if she shall survive me, absolutely and forever.

I wish to specifically state herein that my reason for the bequest of my residuary estate as hereinabove provided is that said William J. McDonald and his said wife have been consistently faithful, both in the affairs of Walter Rose and myself, over a period of years, whereas my other relatives and friends have not given me any valued attention whatsoever.

6. I hereby authorize and empower my Executor, in his or her discretion, to mortgage, sell, exchange or otherwise dispose of any and all real estate, or any interest therein, of which I shall die seized or possessed, in such manner, at such times and on such terms as he or she may deem expedient, and to make, execute and deliver good and sufficient deeds and other conveyances therefor.

7. I hereby nominate, constitute and appoint my said friend, WILLIAM J. McDONALD, the Executor of this my last will and testament; and in the event that he shall not survive me, or fail to qualify, resign or cease to act as such executor for any reason, I hereby nominate, constitute and appoint my friend, ELIZABETH J. McDONALD, his said wife, the Executor of this my last will and testament; and I direct that neither of them shall be required to furnish any bond or undertaking at any time in any jurisdiction for the faithful performance of his duties in such capacity.

8. I hereby revoke all former wills by me at any time made.

IN WITNESS WHEREOF, I have hereunto set my hand and seal this 21st day of August, 1968.

Hazel H. Leckie (L.S.)

Signed, sealed, published and declared by the testator, HAZEL A. LECKIE, as and for her last will and testament, in our presence, and in the presence of each of us, and we, at the same time, at her request, in her presence, and in the presence of each other, hereunto subscribe our names and residences as attesting witnesses, on the 21st day of August, 1968, and at the residence of said testator, at No. 28 College Avenue, in the City of Geneva, New York.

PATRICIA NIXON ADAMS - residing at GENEVA NEW YORK

Arthur C. Adams residing at Geneva, New York

BOOK 333 PAGE 730

CODICIL

to

LAST WILL AND TESTAMENT

of

HAZEL A. LECKIE

I, HAZEL A. LECKIE of the City of Geneva, County of Ontario and State of New York, being of sound mind and memory, do hereby make, publish and declare this to be a first Codicil to my Last Will and Testament heretofore made, signed, published and executed by me and bearing the date August 21, 1968, that is to say:

FIRST: I hereby amend and change my aforesaid Last Will and Testament by revoking subsection "B" of paragraph THIRD.

SECOND: I hereby ratify and republish my Last Will and Testament heretofore executed by me and bearing the date August 21, 1968, except as provided in this First Codicil.

THIRD: Pursuant to Section 1406 of the Surrogate Court Procedure Act and as the same may be amended from time to time hereafter, I request that proof of the attesting witnesses to this my First Codicil may be made and may be taken by an affidavit before any officer authorized to administer oaths stating such facts as could establish the genuineness of my First Codicil, the validity of its execution, the fact of my competency, and freedom from any restraint.

IN WITNESS WHEREOF, I sign, seal, publish and declare this as my First Codicil to my Last Will and Testament in the presence of the persons witnessing it at my request this 5th day of November, 1970.

Hazel A. Leckie (L.S.)
Hazel A. Leckie

Signed, sealed, published and declared by Hazel A. Leckie, the

testatrix above named, to be her first Codicil to her Last Will and Testament, in our presence, and we, at her request and in her presence, and in the presence of each other, have hereunto subscribed our names and witnesses this 5th day of November, 1970.

Anna L. Hardy Residing at Geneva N.Y.

Isabel G. Bloomfield Residing at Geneva N.Y.

COMPROMISE AGREEMENT

THIS AGREEMENT made the 19th day of December, 1972, between WILLIAM J. MC DONALD, residuary legatee under the Last Will and Testament of Hazel A. Leckie dated August 21, 1968 and the Codicil to said instrument dated November 6, 1970, Party of the First Part and JEAN KAUFFMAN of Columbus, Ohio and ANDREW F. LECKIE of Fossil, Oregon, both contingent remaindermen under the provisions of the Trust Agreement set forth in paragraph "4" of said Last Will and Testament and

ETHEL LARSEN	Box 99, Romulus, New York
JOHN ALBRIGHT	Packwood Road, Geneva, New York
CLARENCE ALBRIGHT	601 Glenwood, Syracuse, New York
IDA MAY MOSHER	East Lake Road, Canandaigua, New York
MARY E. OLSCHEWSKE	R. D. #3, Hecker Road, Waterloo, N. Y.
DONALD E. SHERIDAN	Kingdom Road, R. D. #3, Waterloo, N. Y.
LILLIAN F. KAPP	999 Macon Road, Saline, Michigan
EARL R. SHERIDAN	Gifford Road, Phelps, New York

all distributees of the said Hazel A. Leckie, deceased, Parties of the Second Part;

WHEREAS, the said Hazel A. Leckie died on the 28th day of February 1972 a resident of the City of Geneva, County of Ontario leaving a Last Will and Testament dated August 21, 1968 and a Codicil thereto dated November 6, 1970 and

WHEREAS the said Will and Codicil were duly filed in the Surrogate's Court of the County of Ontario together with Petitions praying for its probate and

WHEREAS the parties of the second part filed objections to

the probate of said instruments insofar as the bequest therein to William J. McDonald under Paragraphs "4" and "5" of the Will and to the Codicil insofar as it ratified those paragraphs of the Will and

WHEREAS it appears that the litigation of the issues would engender much publicity and would damage the reputation of William J. McDonald as an attorney,

NOW, THEREFORE, this Agreement

W I T N E S S E T H:

That subject to the approval of the Surrogate of the said County of Ontario and to become effective only as hereinafter stated. the parties hereto do hereby agree as follows:

1. The parties of the second part have withdrawn their objections to the validity of said Will and Codicil and have consented to the probate thereof and have agreed to accept certain sums as hereinafter set forth in consideration therefor and in full settlement of their claims against William J. McDonald and the said estate, and upon receiving said amounts to execute a general release discharging said William J. McDonald and the estate from any and all claims and demands of any kind which they now have or may hereafter have.

Jean Kauffman and Andrew F. Leckie agree to accept and William J. McDonald agrees that they shall be paid one-half of the principal of the Trust Fund set forth under Paragraph "4" of the Last Will and Testament as of the date of appointment of the executor, November 15, 1972, plus all interest accrued on said amount from November 15, 1972 to date of payment, less the pro-rata share of federal and state income and estate taxes, executor's statutory commissions and attorney's fees and disbursements based on the minimum fee schedule of Ontario County.

Ethel Larsen, John Albright, Clarence Albright, Ida May Mosher, Mary E. Olschewske, Donald E. Sheridan, Lillian Frances Rapp and Earl R. Sheridan agree to accept and William J. McDonald agrees that they shall be paid the total sum of Forty Thousand (40,000.00) Dollars. The amount received shall be divided as follows:

Ethel Larsen	20%
John Albright	20%
Clarence Albright	20%
Ida May Mosher	20%
Mary E. Olschewske	5%
Donald E. Sheridan	5%
Lillian F. Rapp	5%
Earl R. Sheridan	5%

2. The executor shall have the right to reserve a reasonable amount from the monies to be paid to Jean Kauffman and Andrew F. Leckie for their share of any possible deficiencies in taxes.

~~[illegible]~~

William J. McDonald

SURROGATE'S COURT ONTARIO COUNTY

In the Matter of the Application for an Order Approving the Compromise of a Controversy Arising in the Estate of

HAZEL A. LECKIE, Deceased.

Petition for Order Approving Compromise of Controversy

TO THE SURROGATE'S COURT OF THE COUNTY OF ONTARIO:

The petition of William J. McDonald, domiciled and residing at No. 870 Pre-Emption Road, in the Town of Geneva, County of Ontario and State of New York, respectfully shows:

1. That your petitioner is the executor named in a paper writing dated the 21st day of August, 1968 purporting to be the last will and testament of Hazel A. Leckie, deceased and in a paper writing dated November 6, 1970 purporting to be a codicil to the last will and testament of said Hazel A. Leckie, deceased.

2. That the said Hazel A. Leckie deceased, at the time of her death was domiciled and resided at No. 28 College Avenue, in the City of Geneva, County of Ontario and State of New York and died on the 28th day of February, 1972.

3. That said paper writings were filed in the Surrogate's Office of the County of Ontario together with petitions praying for their probate and thereafter and on the return day, your petitioner duly appeared in person and respondents duly appeared by John J. Nicit, Esq. and Robert J. Roulan, Esq., their attorneys and filed objections to the probate of said paper writings insofar as to the bequests therein to William J. McDonald, under Paragraphs "4" and "5" of the Will and to the Codicil insofar as it ratified those paragraphs of the Will.

4. That thereafter the respondents withdrew their objections to the validity of the said Will and Codicil and the said Will and Codicil have been probated subject however to an Agreement made between the parties and to the approval of the Surrogate.

5. That the said controversy arising in the said proceeding is now pending undetermined in this Court.

6. That your petitioner and all persons claiming as devisees or legatees under the Will and Codicil and all persons claiming the estate of the said Hazel A. Leckie, deceased, as intestate, are adults and competent and all of said persons are desirous of adjusting by compromise of said controversy and have executed a written agreement effecting an adjustment thereof, subject to the approval of this Court. One of the originals of said agreement is hereto annexed, marked Exhibit "A" and made a part of this petition. To this agreement all persons entitled to or claiming said estate or any interest therein in any manner whatsoever as well as your petitioner have executed said agreement.

7. That the said agreement provides for the adjustment by compromise of said controversy and for the withdrawal of the contest of said Will as set forth hereinabove.

8. That the objections to the probate of the Will and to the Codicil were that the bequests made to William J. McDonald were not freely or voluntarily made by the testatrix, but were procured by the alleged undue influence practiced upon her by William J. Donald. That it appeared that the original Will was prepared under the care and supervision of one Arthur A. Arms, Attorney and that the Codicil was prepared under the care and supervision of William J. McDonald, Attorney. The testimony of the subscribing witnesses to

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the Will and the Codicil have been taken and are part of the records of this Court.

9. That the names and post office addresses of all persons interested in this proceeding are:

Jean Kauffman	Columbus, Ohio
Andrew F. Leckie	Fossil, Oregon
Ethel Larsen	Box 99, Romulus, New York
John Albright	Packwood Road, Geneva, New York
Clarence Albright	601 Glenwood, Syracuse, New York
Ida May Mosher	East Lake Road, Canandaigua, N. Y.
Mary E. Olschewske	R. D. #3, Hecker Road, Waterloo, N. Y.
Donald E. Sheridan	Kingdom Road, R. D. #4, Waterloo, N. Y.
Lillian F. Rapp	999 Macon Road, Saline, Michigan
Earl R. Sheridan	Gifford Road, Phelps, New York.

None of these persons need to be cited as all have signed the Compromise Agreement, Exhibit "A". There are no other persons other than those mentioned, interested in this application or proceeding.

10. That there are no other distributees of the said Hazel A. Leckie, deceased, nor persons entitled to claim the estate of the said deceased or any part thereof under the statutes regulating the descent and distribution of intestate estates except as above stated; that there are no other legatees or devisees named in said Will except as above stated; that there are no persons named as executors or trustees in the said paper writings who have not renounced except as above stated; and that there are no other persons whose interests in the estate are affected by the proposed compromise except as above stated.

11. That there are no other infants, lunatics, persons of unsound mind or habitual drunkards persons under disability or

persons confined in prison interested in or who are necessary parties to the proposed compromise agreement except as above stated and there are no interests of persons unknown or any future contingent interests of persons not in being which are or may be affected by the proposed compromise agreement except as hereinbefore stated.

12. That said Compromise Agreement is such as is favored by the Courts and your petitioner believes it is to the interest and advantage of the decedent and to the legatees and devisees under the said Will, and your petitioner knows that the litigation of the issues would engender much publicity and would endanger the reputation of William J. McDonald as an attorney and if said contest and controversy is not settled, it will, in all probability, be protracted and appeals will be taken to the Appellate Courts, all of which will be expensive and delay the settlement of the estate and will cause a great loss and diminution in value.

WHEREFORE, your petitioner prays that this Court approve and sanction said compromise agreement and authorize your petitioner to adjust by compromise said controversy concerning the validity of said Will and Codicil and authorize, approve and sanction the execution of said compromise agreement by your petitioner and to order that this petition, agreement and releases and any and all other papers pertaining to or referring to this agreement, be sealed and not be subject to access or inspection by any person except by order of the Surrogate for good cause shown and on notice to William J. McDonald, and that the Court set the attorneys' fees to be deducted from the payments to be made to the respondents, and to take such other action and make such orders and decrees as may be necessary to approve and sanction such compromise agreement and make it binding upon all parties

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in interest and for such other and further relief as to the Court may seem just and proper.

William J. McDonald

STATE OF NEW YORK)
: ss.
COUNTY OF ONTARIO)

WILLIAM J. MC DONALD, being duly sworn, deposes and says that deponent is the petitioner in the within action; that deponent has read the foregoing petition and knows the contents thereof; that the same is true to deponent's own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters deponent believes it to be true.

William J. McDonald

Subscribed and Sworn to before me this 12 day of April, 1973.

Notary Public

SALLY A. BRASSFIELD
Notary Public in the State of New York
Ontario County No. 33-0395420
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T. C. Memo. 1977-202

UNITED STATES TAX COURT

WILLIAM J. Mc DONALD, SR., AND ELIZABETH J. Mc DONALD,
Petitioners v. COMMISSIONER OF INTERNAL REVENUE, Respondent.

Docket No. 5160-76. Filed June 29, 1977.

William J. Mc Donald, Sr., pro se.

David R. Smith, for the respondent.

MEMORANDUM OPINION

DAWSON, Chief Judge: Respondent determined the following deficiencies in the petitioners' Federal income taxes:

Taxable Year	Deficiency
1970	$ 6,813.40
1971	8,380.37
1972	1,229.83
1973	17,516.00

The only issue presented for decision is whether petitioners are entitled to a claimed "preservation of reputation" business deduction in the amount of $121,400 for the taxable year 1973. Our determination with respect to that issue will resolve the controversies arising from the taxable years 1970 through 1972 because each concerns a claimed net operating loss carryback from the year 1973. Petitioners filed an amended return for each prior year claiming a refund due to the net operating loss carryback and, although the Internal Revenue Service originally granted petitioners' applications and paid the refunds, the statutory notice of deficiency subsequently was issued for the amount of each refund on the ground that it had been paid in error.

This case was submitted without trial in accordance with the provisions of Rule 122, Tax Court Rules of Practice

and Procedure. We adopt the stipulation of facts and attached exhibits as our findings. The pertinent facts are set forth below.

William J. Mc Donald, Sr., and Elizabeth J. Mc Donald (petitioners) are husband and wife whose legal address was Geneva, New York, at the time their petition was filed herein. They previously had filed timely joint Federal income tax returns for the taxable years 1970 through 1973 with the Internal Revenue Service Center at Andover, Massachusetts.

William J. Mc Donald, Sr. (petitioner) is an attorney who was admitted to the practice of law in the State of New York in 1950. He is now engaged in the practice of law in Geneva, New York.

Hazel A. Leckie, an elderly widow unrelated to the Mc Donalds, executed her last will and testament on August 21, 1968. That document, which made reference to either petitioner, Mrs. Mc Donald, or both of them in several provisions, was not drafted by the petitioner. Mrs. Leckie made the following specific bequests in paragraph 3 of her will:

> C. To my friend, WILLIAM J. McDONALD, an attorney of Geneva, New York, if he shall survive me, my "Booth" painting by John Singer Sargent.

D. To my friend, ELIZABETH J. McDONALD, wife of said attorney, all of my jewelry of every kind and description, and all of my furs, if she shall survive me.

Paragraphs 4 and 5 of the will directed that an existing trust be terminated and its corpus become a part of the decedent's residuary estate, and that the entire residuary estate pass first to petitioner if he survived the decedent, or second to Mrs. Mc Donald if she survived the decedent and petitioner did not:

> 4. Under the provisions of a Trust Agreement, dated July 22, 1965, by and between my late husband, ANDREW F. LECKIE, SR., the grantor, and THE HUNTINGTON NATIONAL BANK OF COLUMBUS, OHIO, the Trustee, I was given a power to direct the disposition of certain property. I hereby exercise the said power of appointment granted to me by said instrument, and direct that all property subject thereto shall become and be a part of my residuary estate, and disposed of as hereinafter provided.
>
> 5. All of the rest, residue and remainder of the property which I may own at the time of my death, real and personal, and including any property over which I may have any power of appointment, I bequeath and devise to my said friend and attorney, WILLIAM J. McDONALD, of Geneva, New York, if he shall survive me, absolutely and forever. In the event that he shall not survive me, I bequeath and devise all of the said residue of my estate to his wife, ELIZABETH J. McDONALD, if she shall survive me, absolutely and forever.
>
> I wish to specifically state herein that my reason for the bequest of my residuary estate as hereinabove provided is that said Willaim J. McDonald and his said wife have been consistently faithful, both in the affairs of Walter Rose and myself, over a period of years, whereas my other relatives and friends have not given me any valued attention whatsoever.

Nothing in the record reveals details concerning the content or value of either the trust corpus or of the entire residuary estate. In paragraph 7 the decedent appointed petitioner the executor of her will, and appointed Mrs. Mc Donald to serve in that capacity if petitioner failed to serve for any reason.

On November 6, 1970, Hazel Leckie amended her original August 21, 1968, will by executing a codicil which revoked a previous specific bequest of $10,000 to a former employee. Petitioner drafted the codicil for Mrs. Leckie. The effect of that alteration was to place an additional $10,000 in the residuary estate which would pass to petitioner or Mrs. Mc Donald pursuant to paragraph 5 of the will.

Mrs. Leckie died on February 28, 1972. When her will was offered for probate, relatives of Mrs. Leckie raised objections to probate alleging that neither the termination of the trust in Paragraph 4 of the will nor the bequest of the residuary estate to petitioner in Paragraph 5 had been made freely or voluntarily. It was alleged that those actions were solely the product of undue influence which petitioner had exerted upon Mrs. Leckie prior to the drafting of her will.

Letters of administration were issued thereafter to petitioner, without bond, by the Surrogate Court of Ontario County, New York, since he had been appointed

executor of Mrs. Leckie's estate by her will. On November 15, 1972, all objections to Mrs. Leckie's will were withdrawn and both the will and codicil were admitted to probate on that date. The objections were withdrawn because petitioner and the will contestants executed a written compromise agreement dated December 19, 1972, which was filed with the Surrogate Court of Ontario County. It was stated in the written agreement that the compromise was reached in part because "it appears that the litigation of the issues would engender much publicity and would endanger the reputation of William J. Mc Donald as an attorney. . . ."

On April 12, 1973, petitioner filed a "Petition for Order Approving Compromise of Controversy" with the Surrogate Court of Ontario County. Subsequently, on April 23, 1973, the Surrogate signed an order approving the proffered compromise agreement. During the remainder of 1973 petitioner paid $121,400 to the heirs and relatives of Mrs. Leckie pursuant to the terms of the compromise agreement. Petitioner made such payments in order to prevent litigation in connection with the will contest proceeding and to avoid any publicity resulting therefrom.

Petitioners claimed a miscellaneous itemized deduction of $121,400 for "preservation of reputation" on Schedule A of their joint Federal income tax return for the year 1973. An explanation of the claimed deduction and copies of two canceled checks payable to BONNEY & NICIT, attorneys for the will contestants, totaling $121,400, were attached to the return. On April 12, 1974, petitioner applied to the Internal Revenue Service for refunds for taxes paid for the taxable years 1970, 1971, and 1972 in the respective amounts of $6,813.40, $8,263.36, and $1,229.83. That application was granted on July 29, 1974, and refunds were paid in the amount of $6,813.40 for 1970, $8,380.37 for 1971, and $1,229.83 for 1972, plus interest. Each of the refund claims resulted from petitioner's claiming a net operating loss carryback from the taxable year 1973 for the year involved. The deficiencies determined by respondent for all four years in issue result entirely from his disallowance of petitioner's $121,400 "preservation of reputation" deduction for 1973, and hence the absence of any loss to carryback to the prior years.

The issue confronting us is strictly one of fact, yet its resolution is not a simple matter because the parties have provided the Court with minimal information, and the concept of "undue influence," without further illumination, can be used in reference to many diverse

forms of conduct. Nonetheless, on this record, we think the petitioner has established that he is entitled to deduct the entire amount pursuant to the provisions of section 162(a), Internal Revenue Code of 1954.[1]

Petitioner's presentation is simple and straightforward. He is, and was for many years prior to the years in issue, an attorney actively engaged in the practice of law. Hazel A. Leckie, an elderly widow, occasionally called upon petitioner to perform legal services for her. Mrs. Leckie also considered petitioner and Mrs. Mc Donald to be her close friends. Upon her death in 1972, petitioner and Mrs. Mc Donald stood to receive several bequests from Mrs. Leckie through the probate of her will. Petitioner had not drawn the will for Mrs. Leckie. However, several of the decedent's relatives contested the probate of her will on the ground that petitioner had practiced undue influence upon her and thereby wrongfully caused her to bequeath funds to him that otherwise <u>might have</u> passed to them.

Alarmed over the possible damage that a hotly contested,

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1. Except as otherwise indicated, all statutory references herein pertain to the Internal Revenue Code of 1954, as amended during the years in issue.

vengeful lawsuit could cause to his professional reputation as a lawyer, petitioner quickly compromised the suit and paid $121,400 to the various claimants. That amount was later deducted on petitioner's Federal income tax return for 1973, and formed the basis for all three refund claims for prior years.

Respondent disallowed petitioner's "preservation of reputation" deduction in its entirety, and issued a statutory notice of deficiency for that year and the three preceding years to which excess net operating losses had been carried back. Citing the Supreme Court's decision in Welch v. Helvering, 290 U.S. 111 (1933), respondent characterizes petitioner's expenditures as nondeductible personal expenses within the meaning of section 262 of the Code on the grounds that (1) the payments were not "directly connected" with petitioner's trade or business, (2) nothing in the record indicates that petitioner's fears of damage to his professional reputation were justified, and (3) petitioner made the payments primarily to preserve some portion of his inheritance from Mrs. Leckie rather than to protect his business.

Section 162(a) provides, in pertinent part, that "There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the

taxable year in carrying on any trade or business * * * ." These is no question that the active practice of law constitutes a "trade or business" within the meaning of section 162. See, e.g., Pepper v. Commissioner, 36 T.C. 886 (1961); Snow v. Commissioner, 31 T.C. 585 (1958). There is likewise no question that petitioner was engaged in the active practice of law, and that an attorney-client relationship existed between petitioner and Mrs. Leckie at all times prior to her death. While it may be true that petitioner and Mrs. Leckie, and indeed Mrs. Mc Donald and Mrs. Leckie, were also close friends, this fact in no way diminishes the obvious simultaneous professional relationship that existed between them. Respondent argues to the contrary and seeks support for his claim from the fact that petitioner did not draft Mrs. Leckie's will. We do not find that argument persuasive because petitioner, as a beneficiary under the will, might have violated his profession's code of ethics by the act of drafting Mrs. Leckie's will. The record indicates that petitioner had known Mrs. Leckie for years, that she selected him to act as the executor of her will, that at a later date she selected him to draft the codicil to her will, and that he is described by her in paragraph 5 of her will as "my said friend and attorney." In addition, we note that not only was petitioner consistently described

in the will as an attorney, he also was the only individual identified by trade or profession.

It is clear that claims of "undue influence" arising out of a professional relationship of a confidential nature could undermine the public's confidence or trust in an attorney. This seems true even where the claimants are presumably irate individuals who, until the recent reading of a will, expected to take large sums of money upon the termination of a trust to which they were contingent remaindermen. Further exacerbating this situation is the fact that the one individual who could answer such allegations, Mrs. Leckie, died prior to the prosecution of such claims. Petitioner has resolutely asserted from the moment of settlement of those claims that he settled them solely to nip any litigation in the bud and thereby reduce any possible adverse publicity to a minimum. In our judgment the alleged breach of trust underlying the will contest suit was directly connected with petitioner's practice of law, whether or not it ever actually occurred. Moreover, we think the petitioner's primary purpose for settling those claims was to protect his business reputation and his future earnings flow. His personal considerations were incidental to his desire to protect his business. This is true even though the form of the legal action was a will contest

suit rather than an action brought directly against petitioner, because either could bring about the results petitioner feared.

Respondent contends that petitioner compromised the suit and insured probate of Mrs. Leckie's will primarily to preserve some portion of his inheritance. The record does not support that argument. As stated above, situations of this nature often will not produce large quantities of independent corroborative evidence of primary intentions. The only evidence before us supports petitioner's assertion that he acted to protect his business reputation and future earnings. Respondent's case dwells entirely upon suspicions and unsupported allegations. Therefore, we find that petitioner has carried his burden of proof.

Two cases decided by the United States Court of Appeals for the Second Circuit bolster petitioner's claim despite several factual differences. In Levitt & Sons v. Nunan, 142 F. 2d 795 (2d Cir. 1944), the taxpayer paid another corporation $65,000 to secure a release from its claim involving a purported breach of trust by a former officer of that corporation. That person currently served as an officer of the taxpayer. The taxpayer-corporation was involved in many complex

business dealings at the time the claim was made and, fearful that public knowledge of the claim would damage its business, paid the alleged damages despite its belief that the claim was utterly baseless and deducted that payment on its tax return as an expense item. The Court of Appeals stated with respect to the deduction:

> That such payments to protect a business generally are "ordinary" expenses is abundantly settled by authority and can no longer be questioned. . . . An expense to avoid such results may be "necessary," although the anticipated loss is not inevitable; business, like everything else, can only be conducted upon prophecies, and prophecies are never infallible. [citations omitted.] 142 F. 2d at 799.

In an earlier case before that same Court, Helvering v. Community Bond & Mortgage Corp., 74 F. 2d 727 (2d Cir. 1935), a corporate taxpayer was permitted to deduct as a business expense the costs associated with preserving its business reputation and future earnings because its "primary motive" was found to be the preservation of that reputation. In our opinion the petitioner's actions fall within the spirit, if not the factual pattern, of these cases.

Decision will be entered for the petitioners.

UNITED STATES TAX COURT
WASHINGTON, D.C. 20217

WILLIAM J. Mc DONALD, SR., AND ELIZABETH J. Mc DONALD, Petitioner, v. COMMISSIONER OF INTERNAL REVENUE, Respondent.	Docket No. 5160-76.

DECISION

Pursuant to the determination of the Court, as set forth in its Memorandum Opinion, (T. C. Memo. 1977-202), filed June 29, 1977, it is

ORDERED AND DECIDED: That there are no deficiencies in petitioners' Federal income taxes for the calendar years 1970, 1971, 1972, and 1973.

(Sig.) Howard A. Dawson, Jr.

Howard A. Dawson, Jr.
Chief Judge

Entered: JUN 30 1977

CERTIFICATE OF SERVICE

It is hereby certified that service of the foregoing Appendix has been made on appellee, appearing pro se, by mailing four copies thereof to him on this 19th day of December, 1977, in an envelope, with postage prepaid, properly addressed to him as follows:

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